FILE COPY

Office-Supreme Court, U.S.
FILED
APR 6 1959
[illegible], Clerk

No. 769

In the Supreme Court of the United States

OCTOBER TERM, 1958

DAVID SIEBEN III ET AL., PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

J. LEE RANKIN,
Solicitor General,
CHARLES K. RICE,
Assistant Attorney General,
[illegible],
[illegible] W. BRADY,
Attorneys,
Department of Justice, Washington 25, D.C.

INDEX

	Page
Opinions below	1
Jurisdiction	1
Question presented	1
Statute and Regulations involved	2
Statement	3
Argument	6
Conclusion	8

CITATIONS

Cases:	
Corn Products Co. v. *Commissioner*, 350 U.S. 46	7
Warner Bros. Pictures v. *Columbia Broadcasting System*, 216 F. 2d 945, certiorari denied, 348 U.S. 971	7–8
Statutes:	
Internal Revenue Code of 1939:	
Sec. 22(a) (26 U.S.C. 22(a))	2
Sec. 117(a) (26 U.S.C. 117(a))	2, 6, 7
Revenue Act of 1950, c. 994, 64 Stat. 906, Sec. 210(c)	6
Miscellaneous:	
H. Rep. No. 2319, 81st Cong., 2d Sess., pp. 54, 91–92 (1950–2 Cum. Bull. 380, 420–421, 445–446)	7
S. Rep. No. 2375, 81st Cong., 2d Sess., pp. 83–84 (1950–2 Cum. Bull. 483, 543)	7
Treasury Regulations 118, Sec. 39.117(a)–1	3

501483—59

In the Supreme Court of the United States

OCTOBER TERM, 1958

No. 759

DAVID STERN III ET AL., PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the District Court (Pet. 9–20) is reported at 164 F. Supp. 847. The opinion of the Court of Appeals (Pet. 20–21) is not yet officially reported.

JURISDICTION

The judgment of the Court of Appeals was entered on February 18, 1959, and the petition for a writ of certiorari was filed on March 9, 1959. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1254(1).

QUESTION PRESENTED

Whether the consideration taxpayer received during the years 1951–1953 for the sale of his entire

interest in certain literary property created by him was taxable as ordinary income rather than as capital gain by virtue of Section 117(a)(1)(C) of the Internal Revenue Code of 1939.

STATUTE AND REGULATIONS INVOLVED

Internal Revenue Code of 1939:

SEC. 22. GROSS INCOME.

(a). *General Definition.*—"Gross income" includes gains, profits, and income derived from * * * dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; * * * or gains or profits and income derived from any source whatever. * * *

* * * * * *

(26 U.S.C. 22)

SEC. 117. CAPITAL GAINS AND LOSSES.

(a) *Definitions.*—As used in this chapter—

(1) [As amended by Sec. 210, Revenue Act of 1950, c. 994, 64 Stat. 906] *Capital assets.*—The term "capital assets" means property held by the taxpayer (whether or not connected with his trade or business), but does not include—

* * * * *

(C) a copyright; a literary, musical, or artistic composition; or similar property; held by—

(i) a taxpayer whose personal efforts created such property, or

* * * * *

(26 U.S.C. 117)

Treasury Regulations 118, promulgated under the Internal Revenue Code of 1939:

> SEC. 39.117(a)–1 *Meaning of terms.* (a) The term "capital assets" includes all classes of property not specifically excluded by section 117(a)(1). In determining whether property is a "capital asset", the period for which held is immaterial.
>
> * * * * * *
>
> (c) A copyright, a literary, musical, or artistic composition, and similar property are excluded from the term "capital assets" if held by a taxpayer whose personal efforts created such property, or if held by a taxpayer in whose hands the basis of such property is determined, for the purpose of determining gain from a sale or exchange, in whole or in part by reference to the basis of such property in the hands of the person whose personal efforts created such property. As to the application of section 117(j) to the sale or exchange of such property held by such a taxpayer, see Sec. 39.117(j)–1. The phrase "similar property" includes, for example, such property as a theatrical production, a radio program, a newspaper cartoon strip, or any other property eligible for copyright protection (whether under statute or common law), but does not include a patent or an invention, or a design which may be protected only under the patent law and not under the copyright law.
>
> * * * * * *

STATEMENT

During World War II, while the taxpayer was stationed in Hawaii as an Army officer, he wrote

several pages of imaginary dialogue between a lonely second lieutenant and an Army mule named Francis. The dialogue, which was a satire on Army life, was printed in an Army newspaper, and Francis the talking mule quickly became a popular figure. Taxpayer wrote additional dialogue for the Army paper, and he also wrote several short stories concerning Francis which he later sold to various magazines. (Pet. 9–10; R. 122.)[1]

After he was discharged from the Army, taxpayer wrote and obtained a statutory copyright on two novels entitled "Francis" and "Francis Goes to Washington". Both novels were sold to and published by Farrar-Strauss. In 1947, taxpayer sold the motion picture rights to the first novel to an independent producer, and in turn, the producer assigned his rights to Universal Pictures Company. Using a screen play written by taxpayer, Universal produced the motion picture "Francis" in 1949. (Pet. 10; R. 123–124.)

On June 2, 1950, taxpayer entered into a contract with Universal Pictures Company whereby taxpayer sold to Universal (Pet. 10; R. 126–128):

> 1. All his rights in the character known as Francis which he had conceived and created;
>
> 2. All his rights in the novels "Francis" and "Francis Goes to Washington" which he had written and copyrighted, including the titles, themes and contents of the novels, as well as the copyrights and renewal rights; and
>
> 3. All his rights accruing under prior con-

[1] Record references are to the record in the Court of Appeals.

tracts with other parties involving the above subject matter.

As consideration for the transfer, Universal agreed to pay taxpayer a fixed fee of $50,000, a share of all profits accruing under the prior contracts dealing with Francis, and $50,000 plus a share of the profits on each motion picture which Universal thereafter produced using the character Francis. (Pet. 10–11; R. 135–144.) Universal subsequently produced six such pictures. (Pet. 11; R. 124.)

On their joint returns for the years 1950–1953, taxpayer and his wife treated the amounts received from Universal pursuant to the above provisions of the contract as capital gains in the year of receipt. (Pet. 11–12; R. 125.)[2] The Commissioner determined that the amounts taxpayer received from Universal were ordinary income, and after paying the deficiencies determined by the Commissioner, taxpayer and his wife brought suit for a refund. The District Court allowed the refund claimed for the year 1950, but held that the proceeds received by taxpayer during the years 1951–1953 were taxable as ordinary income by virtue of Section 117(a)(1)(C) of the Internal Revenue Code of 1939, which was added to the Code by the Revenue Act of 1950. (Pet. 9–20.) Taxpayer and his wife appealed with respect to the years 1951–1953, and the Court of Appeals affirmed in a *per curiam* opinion. (Pet. 20–21.)

[2] Under the contract with Universal, taxpayer was also entitled to write screen plays for each Francis motion picture at a compensation of $10,000 per screen play. (R. 144–145.) The amounts taxpayer received for this work were reported as ordinary income. (R. 125.)

ARGUMENT

This is a case of first impression, the decision below is correct, and further review is not warranted.

1. Section 117(a)(1)(C) of the Internal Revenue Code of 1939, *supra*, p. 2, was added to the Code in 1950 to deny capital gain treatment to income derived from the sale of "a copyright; a literary, musical, or artistic composition; or similar property" held by "a taxpayer whose personal efforts created such property". The taxpayer in the case at bar created a fictional character in the process of writing numerous short stories and two copyrighted novels. Having created a character with popular appeal, taxpayer was able to sell his interest in the character and the novels to a motion picture company. (Pet. 10–11; R. 127–128.) The courts below were clearly correct in holding that the sales proceeds which taxpayer received in the years 1951–1953 were taxable as ordinary income, rather than as capital gain, by virtue of Section 117(a)(1)(C).[2]

Taxpayer's contention (Pet. 7) that the sale of a fictional character is not covered by the statute runs counter to the plain language and history of Section 117(a)(1)(C) and finds no support in any decision. Under taxpayer's view, income from the sale of a book is taxable at ordinary income rates, but income from the sale of a character in the same book is taxable at the preferential capital gain rates. Congress

[2] These provisions apply to the amounts received in the years 1951–1953, even though the sale in question took place prior to the enactment of Section 117(a)(1)(C). See Pet. 19, fn. 12, and Section 210(e) of the Revenue Act of 1950.

clearly did not intend or expect such an incongruous result when it provided in Section 117(a)(1)(C) that the ordinary income rates would apply in all cases where the creator of "a literary, musical, or artistic composition; or similar property" sold his creative work. In view of the obvious purpose of the statute, the language used by Congress is certainly broad enough to cover the case where the author of a literary composition sells it together with his interest in the principal character. Cf. *Corn Products Co.* v. *Commissioner*, 350 U.S. 46, 52. See also H. Rep. No. 2319, 81st Cong., 2d Sess., pp. 54, 91–92 (1950–2 Cum. Bull. 380, 420–421, 445–446); S. Rep. No. 2375, 81st Cong., 2d Sess., pp. 83–84 (1950–2 Cum. Bull. 483, 543).

As the District Court indicated (Pet. 17–18), taxpayer's assertion (Pet. 7–8) that a fictional character can not be copyrighted is beside the issue, because there is nothing in the statute or the Regulations, *supra*, p. 3, to indicate that Section 117(a)(1)(C) applies exclusively to property which is eligible for copyright protection. Whether or not the central character of a book can be copyrighted as such, the sale of the author's interest in that character stands on the same footing tax-wise as a sale of the book itself, and the courts below were clearly correct in so holding. (Pet. 18–21.)

2. As taxpayer points out (Pet. 6), this is the first decided case involving the provisions of Section 117(a)(1)(C), and quite obviously, there is no conflict. Taxpayer's reliance (Pet. 2, 6–7, 8) on *Warner Bros. Pictures* v. *Columbia Broadcasting System*, 216 F.

2d 945 (C.A. 9), certiorari denied, 348 U.S. 971, a copyright infringement suit, is completely misplaced. No question of tax law was there involved, and in holding that a book and the central character in the book could be sold separately by the author, the court said nothing to suggest that the sales would be subject to different tax treatment.[4]

CONCLUSION

For the reasons stated, the petition for a writ of certiorari should be denied.

Respectfully submitted.

J. LEE RANKIN,
Solicitor General.
CHARLES K. RICE,
Assistant Attorney General.
HARRY BAUM,
GEORGE W. BEATTY,
Attorneys.

APRIL, 1959

[4] Moreover, the decision turned upon construction of a contract the terms of which differed materially from the contract here involved, the court holding that the author had not conveyed his interest in the characters used in his writings. Here, the taxpayer admittedly sold his right to both the novels and the characters. (Pet. 10–11, 18.)

U. S. GOVERNMENT PRINTING OFFICE 1959